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No. _____

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In The

Supreme Court of the United States

October Term, 1991

WESTERN FARM CREDIT BANK,

Petitioner,

v.

ELMER FOBIAN AND ELSE FOBIAN,

Respondents.

Petition For Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

In a federal bankruptcy proceeding involving a creditor's successful objection to a solvent debtor's plan of reorganization, did the Ninth Circuit err in creating an unwritten, *per se*, federal rule that a contractual attorneys' fee provision (that is otherwise enforceable under state law) is inapplicable in bankruptcy when "the litigated issues involve not basic contract enforcement questions, but issues peculiar to federal bankruptcy law"?

LIST OF PARTIES

The parties to the proceeding below were the Petitioner, Western Farm Credit Bank, and the Respondents, Elmer Fobian and Else Fobian. Western Farm Credit Bank is a federally chartered instrumentality of the United States and is part of the federal Farm Credit System. 12 U.S.C. §§ 2001 *et seq.*

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PETITION FOR WRIT OF CERTIORARI

Western Farm Credit Bank, the Petitioner herein, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Ninth Circuit entered in the above entitled case on December 24, 1991.

OPINIONS BELOW

The December 24, 1991, opinion of the Court of Appeals for the Ninth Circuit affirms the judgment of the Bankruptcy Appellate Panel of the Ninth Circuit reversing the judgment of the bankruptcy court. The opinion is

reported at *In Re Fobian*, 951 F.2d 1149 (9th Cir. 1991). The Court of Appeals for the Ninth Circuit denied Western Farm Credit Bank's Petition for Rehearing on February 4, 1992. The Ninth Circuit's Opinion and the Order denying the Petition for Rehearing are reprinted as Appendix A to this Petition at App. 1.

On August 16, 1990, the Ninth Circuit Bankruptcy Appellate Panel ("BAP") entered its Memorandum reversing the bankruptcy court's confirmation of the Respondents' Chapter 12 Plan. The BAP's decision was appealed by the Respondents to the Ninth Circuit Court of Appeals. The BAP's Memorandum was not published and is reprinted as Appendix B to this Petition at App. 12.

The Memorandum Opinion and Order Including Findings of Fact and Conclusions of Law of the Bankruptcy Court for the Eastern District of California confirming Respondent's Chapter 12 plan was entered on August 7, 1989. The Order of Confirmation of Debtor's Plan at Reorganization was entered on August 25, 1992. The bankruptcy court's opinion was not published and the Opinion and the Order of Confirmation are reprinted as Appendix C to this Petition at App. 24.

JURISDICTION

The judgment of the Court of Appeals for the Ninth Circuit was entered on December 24, 1991, affirming the judgment in favor of the Petitioner entered by the Bankruptcy Appellate Panel. Petitioner's Petition for Rehearing was denied on February 4, 1992. This court's jurisdiction is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTES INVOLVED

This case arose from Petitioner's – a creditor of Respondents who are in Chapter 12 bankruptcy – successful efforts to oppose confirmation of Respondents' Chapter 12 plan. Petitioner opposed confirmation of the plan under Sections 1225(a)(4) and 1225(b)(1)(A) of the Bankruptcy Code, Title 11 of the United States Code. 11 U.S.C. § 1225(a)(4) provides, in relevant part:

> Except as provided in subsection (b), the court shall confirm a plan if –
>
> . . .
>
> (4) the value, as of the effective date of the plan, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such a claim if the estate of the debtor were liquidated under chapter 7 of this title on such date; . . . .

11 U.S.C. § 1225(b)(1)(A) provides in relevant part:

> If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan unless, as of the effective date of the plan –
>
> (A) the value of the property to be distributed under the plan on account of such claim is not less than the amount of such claim.

While the Ninth Circuit affirmed the Bankruptcy Appellate Panel's reversal of the confirmation of Petitioner's plan, the Ninth Circuit denied Petitioner's request for attorneys' fees that were otherwise recoverable under

state law pursuant to a contractual attorneys' fees provision. Petitioner believes that its attorneys' fee provision is enforceable in bankruptcy and that its fees should be made part of its allowed unsecured claim. 11 U.S.C. § 506(a) defines secured and unsecured claims. Section 506(a) provides as follows:

> An allowed claim of a creditor secured by a lien on property in which the estate has an interest, or that is subject to setoff under section 553 of this title, is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property, or to the extent of the amount subject to setoff, as the case may be, and is an unsecured claim to the extent that the value of such creditor's interest or the amount so subject to setoff is less than the amount of such allowed claim. . . .

Secured creditors are generally allowed to recover attorneys' fees, if provided by their contract, up to the amount of their security under 11 U.S.C. § 506(b), which provides as follows:

> To the extent that an allowed secured claim is secured by property the value of which, after any recovery under subsection (c) of this section, is greater than the amount of such claim, there shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs, or charges as provided for under the agreement under which such claim arose.

The allowance of claims generally is governed by 11 U.S.C. §§ 502(a) and (b), which provide in relevant part:

> (a) A claim or interest, proof of which is filed under section 501 of this title, is deemed

> allowed, unless a party in interest . . . objects.
>
> (b) . . . [I]f such objection to a claim is made, the court, after notice and hearing, shall determine the amount of such claim . . . and shall allow such claim in such amount except to the extent that –
>
> (i) such claim is unenforceable against the debtor and property of the debtor, under any agreement or applicable law for a reason other than because such claim is contingent or unmatured . . . .

Respondents are solvent Chapter 12 debtors. 11 U.S.C. § 726(a)(5) provides that post-petition interest on claims be paid if the funds are available. 11 U.S.C. § 726(a)(5) provides, in relevant part:

> Except as provided in section 510 of this title, property of the estate shall be distributed –
>
> . . .
>
> (5) Fifth, in payment of interest at the legal rate from the date of the filing of the petition, on any claim paid under paragraph (1), (2), (3), or (4) of this subsection . . . .

Petitioner's promissory note and deed of trust are governed by California law. Attorneys' fees provisions in contracts in California are enforceable under Cal. Civil Code § 1717(a) which provides as follows:

> In any action on a contract, where the contract specifically provides that attorneys' fees and costs, which are incurred to enforce that contract, shall be awarded either to one of the parties or to the prevailing party, then the party

> who is determined to be the party prevailing on the contract, whether he or she is the party specified in the contract or not, shall be entitled to reasonable attorneys' fees in addition to other costs.
>
> . . .
>
> Reasonable attorneys' fees shall be fixed by the court and shall be an element of the costs of suit. . . .

I.

STATEMENT OF THE CASE

This case involves the proper interplay of the Bankruptcy Code and state law relating to the allowance of a creditor's claim for attorneys' fees incurred in bankruptcy proceedings. In broadly devising a *per se* rule that a contractual attorneys' fee provision is inapplicable when "the litigated issues involve not basic contract enforcement questions, but issues peculiar to federal bankruptcy law," the Ninth Circuit went far beyond the language and purpose of the Bankruptcy Code, and even undermined the clear language of 11 U.S.C. § 506(b) in holding that, notwithstanding a contractual attorneys' fees clause, "where the litigated issues involve not basic contract enforcement questions, but issues peculiar to federal bankruptcy law, attorneys' fees will not be awarded absent bad faith or harassment by the losing party." *In re Fobian*, 951 F.2d 12149, 1153 (9th Cir. 1991).

The Fobians are solvent Chapter 12 debtors. They were current on all obligations except a loan from petitioner Western Farm Credit Bank ("the Bank"). The Bank

holds a promissory note secured by 70.5 acres of land located in Glenn County, California. The promissory note executed by the Fobians in favor of the Bank provides for reimbursement of attorneys' fees and costs to the prevailing party. The promissory note provides:

> Each of the undersigned . . . agrees to pay reasonable attorneys' fees and costs incurred in collection of payment due, or in the enforcement of any right or remedy hereunder.

The deed of trust executed by the Fobians in favor of the Bank also contains a provision for attorneys' fees. The deed of trust provides:

> (3) Beneficiary may . . . (b) appear in and litigate any matters, *including condemnation and bankruptcy proceedings*, affecting the security of lien, and may incur necessary costs, expenses, and attorneys' fees therefor . . . which advances, together with interest accrued thereon shall be immediately due and payable . . . . (Emphasis added.)

After the Fobians filed their Chapter 12 petition, the Bank filed a Proof of Claim for $191,660.09. The Fobians made no objection to this Proof of Claim. The Fobians' plan asserted that the Bank's collateral was worth only $70,500. Under the normal application of 11 U.S.C. § 506(a), the Bank would have an allowed secured claim to the extent of the value of the collateral as determined by the bankruptcy court, and an allowed unsecured claim for the remainder.

The Fobians submitted their "First Amended Plan for Reorganization under Chapter 12" (the "Plan"). The Bank filed objections to the Plan, and a confirmation hearing

was held on June 27, 1989. The Bank objected to confirmation of the Plan on the grounds that the Plan made no provision for payment of the unsecured portion of the Bank's claim (the deficiency between the amount of the debt and the value of the collateral) and thus did not comply with Section 1225(a)(4). The Bankruptcy Court nonetheless confirmed the Plan in a Memorandum Opinion and Order Including Findings of Fact and Conclusions of Law filed on August 7, 1989.

The Bankruptcy Appeal Panel ("BAP") reversed, holding that, because the Plan did not meet the requirements of Section 1225, it could not be confirmed. The Fobians appealed the BAP decision to the Ninth Circuit. The Bank argued for affirmance of the BAP's decision, and asked that the Ninth Circuit award it attorneys' fees and costs. The Ninth Circuit affirmed the BAP's decision, awarded the Bank its costs on appeal, but denied the Bank's request for attorneys' fees, despite the contractual provision in the loan documents for an award of fees, on the ground that "where the litigation issues involve not basic contract enforcement questions, but issues peculiar to federal bankruptcy law, attorney's fees will not be awarded absent bad faith or harassment by the losing party." 951 F.2d at 1153.

In refusing to allow a claim for fees, the Ninth Circuit provided no guidance as to when a creditor's ordinary activities in a bankruptcy involve issues "peculiar to federal bankruptcy law." Petitioner's activities here were commonplace – objecting to a plan that failed to provide for any payment of a portion of Petitioner's claim. The Ninth Circuit described this activity of defending a claim

as follows: "[T]he Bank sought proper application of Sections 506 and 1225. This was not a traditional 'action on the contract.' " *Id.* This overly broad rule, which finds no written basis in Section 506 or elsewhere in the Bankruptcy Code, throws into confusion the allowance of all claims for fees incurred by creditors in bankruptcy proceedings.

II.

REASONS FOR GRANTING THE WRIT

This case is a symptom of the Ninth Circuit's confusion over the statutory basis for the award of post-petition attorney's fees in bankruptcy proceedings. Until *Fobian*, there at least was agreement that, under the plain language of 11 U.S.C. § 506(b), a secured creditor may recover its reasonable attorneys' fees up to the value of its security if attorney's fees are provided for in the parties' underlying contract. However, the Bankruptcy Code is silent as to whether an undersecured or unsecured creditor may make its post-petition attorneys' fees part of its unsecured claim. Out of this silence, a cacophony of disagreement has arisen from the courts, and the *Fobian* ruling is so overbroad that it undermines the literal language of Section 506(b) and casts doubt even on whether a fully secured creditor may recover fees under Section 506(b) when the litigated issues involve federal bankruptcy law rather than basic contract enforcement issues. *Fobian* is an unwarranted departure from the "American Rule" for attorneys' fees, and encourages forum-shopping in what should be a national bankruptcy scheme.

The cases which addressed this question under the former Bankruptcy Act held that where a creditor makes a claim under a contract which provides for the recovery of attorneys' fees, post-petition attorneys' fees are added to the creditor's unsecured claim. *See, e.g., In re United Merchant and Mfrs., Inc.*, 674 F.2d 134 (2nd Cir. 1982). In *United Merchant*, the Second Circuit even stated that it thought that there was nothing in the provisions of the new Bankruptcy Code (which became effective in 1979) which would change this rule. *United Merchant, supra*, 674 F.2d at 138.

In deciding the same question under the current Bankruptcy Code, some courts have followed the former Bankruptcy Act rule and have made post-petition attorneys' fees part of a creditor's unsecured claim. *Transouth Financial Corp. of Florida v. Johnson*, 931 F.2d 1505, 1507 (11th Cir. 1991); *In re Martin*, 761 F.2d 1163, 1168 (6th Cir. 1985). However, other courts have departed from this rule and denied the creditor's request that post-petition attorneys' fees became part of its allowed claim. The courts which have denied claims for attorneys' fees have generally done so on two grounds. The first group has read 11 U.S.C. § 506(b) as to the exclusive basis for a claim for fees, and read Section 506(b) to limit the recovery of attorneys' fees to oversecured creditors. *See, e.g., In re Sakowitz*, 110 B.R. 268, 275 (Bankr. S.D. Tex. 1989). The second group has held that where the question before the court is one of federal bankruptcy law rather than contract enforcement, attorneys' fees will not be awarded. *See, e.g., In re Coast Trading Co., Inc.*, 744 F.2d 686, 693 (9th Cir. 1984); *compare, In Re J.F. Hink & Son*, 815 F.2d 1314,

1318 (9th Cir. 1987) (fees awarded for litigating a dispute over Section 365 of the Bankruptcy Code).

In *Fobian*, the Ninth Circuit correctly begins its analysis of the attorneys' fees claim with the statement that awards of attorneys' fees in bankruptcy are governed by state law. However, without any analysis of the application of state law in bankruptcy proceedings, the Court then announces an unwritten, *per se* rule *against* the award of attorneys' fees as part of a creditor's claim in bankruptcy proceedings where the litigated issues are "peculiar to bankruptcy law" rather than are "basic contract enforcement questions." The Ninth Circuit's broad rule not only conflicts with the history of attorneys' fees in general, but also creates a conflict with the Sixth Circuit, the Eleventh Circuit, the Southern District of New York, the Western District of Kentucky, and the Bankruptcy Court for the Northern District of Texas. See, *Transouth Financial Corp. of Florida v. Johnson*, 931 F.2d 1505, 1507 (11th Cir. 1991); *In re Martin*, 761 F.2d 1163, 1168 (6th Cir. 1985); *Liberty National Bank v. George*, 70 B.R. 312, 317 (W.D. Kentucky 1987); *In re Ladycliff College*, 56 B.R. 765, 769 (S.D.N.Y. 1985); *In re Missionary Baptist Foundation of America, Inc*, 24 B.R. 970, 971 (Bankr. N.D. Tex. 1982). Additionally, the *Fobian* rule cannot be harmonized with the Ninth Circuit's own ruling in *In Re J.F. Hink & Sons*, 815 F.2d 1314, 1318 (9th Cir. 1987).

The Ninth Circuit has created unneeded confusion among participants in bankruptcy proceedings. This conflict must be resolved, as the issue is one that is integral to a national bankruptcy law that is intended to be uniformly applied to avoid forum shopping and the coincidence of jurisdiction determining the outcome of a

material issue in a particular case. The Ninth Circuit's creation of a *per se* rule without guidance as to which "issues peculiar to bankruptcy law" it applies to, and what attorneys' fee rule it is interpreting, leaves every participant in federal bankruptcy proceedings in a precarious position with no means of determining whether attorneys' fees will be recoverable or how such a determination is to be made. This confusion will, of itself, cause more attorneys' fees to be incurred. This issue, which presents itself in almost every bankruptcy proceeding, should not be the subject of conflicts among the courts or indefiniteness within them.

The Ninth Circuit's *per se* rule is wrong for a number of reasons. First, no court has ever interpreted Section 506(b) to deny a fully secured creditor a claim for its attorneys' fees on the grounds that the litigated issues were "peculiar to federal bankruptcy law." *See, e.g., In re McGaw Property Management, Inc.*, 133 B.R. 227, 229-230 (Bankr. C.D. Cal. 1991) (under 506(b), award of attorneys fees is *mandatory* if creditor is oversecured and fees are provided for in the underlying agreement). The broad rule enunciated in *Fobian* now encourages disputes over fees if the issues litigated were "peculiar to federal bankruptcy law."

Second, *Fobian* provides no criteria to determine what are issues peculiar to federal bankruptcy law. The few prior cases which have denied attorneys' fees on the grounds that the litigated issues were peculiar to bankruptcy law involved very narrow issues as to the threshold applicability of bankruptcy proceedings to the creditor's claim. *See, e.g., In re Coast Trading Co., Inc.*, 744 F.2d 686 (9th Cir. 1984). The Ninth Circuit's newly-created

inclusion in *Fobian* of a creditor's ordinary attempt under Section 506 and 1225 to defend its unsecured claim in the category of cases which deal with issues "peculiar to bankruptcy law" leaves essentially *no* activity by a creditor beyond attack by a debtor or trustee.

Third, the refusal to make attorneys' fees part of a creditor's claim is a departure from the "American Rule" which governs the award of attorneys' fees in federal courts. Under the "American Rule," each party pays its own fees unless there is an enforceable contract which provides for them. *Alyeska Pipeline Service Co. v. Wilderness Society*, 421 U.S. 240, 257, 95 S. Ct. 1612, 1621, 44 L. Ed. 2d 141 (1975). The Ninth Circuit, through its ruling in *Fobian*, has declared that even when a contract expressly provides for attorneys' fees resulting from bankruptcy proceedings to be recovered, that clause is unenforceable. The Ninth Circuit's rule goes beyond the Bankruptcy Code's written provisions and is at odds with previous bankruptcy law on attorneys' fees, and with federal law (the American Rule) on the award of attorneys' fees in general.

III.

THE NINTH CIRCUIT'S RULING IS IN CONFLICT WITH DECISIONS OF THE SIXTH AND ELEVENTH CIRCUITS AND VARIOUS DISTRICT AND BANKRUPTCY COURTS

The Ninth Circuit's decision to deny post-petition attorneys' fees in *Fobian* is in conflict with decisions in other federal courts. In *In re Martin*, 761 F.2d 1163 (6th Cir. 1985) the Sixth Circuit held that "[C]reditors are entitled to recover attorneys' fees in bankruptcy claims if

they have a contractual right to them under state law, ... " *Id.* at 1168. The Eleventh Circuit has awarded attorneys' fees incurred in a successful non-dischargeability proceeding. *Transouth Financial Corp. of Florida v. Johnson*, 931 F.2d 1505, 1507-1508 (11th Cir. 1991). The Eleventh Circuit's ruling in *Transouth Financial* is especially telling because non-dischargeability proceedings are used as an example by the Ninth Circuit in *Fobian* of proceedings which involve issues peculiar to federal bankruptcy law for which fees would *not* be awarded. *Fobian*, 951 F.2d at 1153. *Fobian* is even at odds with another Ninth Circuit ruling, *In Re J.F. Hink & Sons*, 815 F.2d 1314 (9th Cir. 1987), in which fees were awarded in a dispute arising under Section 365 of the Bankruptcy Code, which is one of the few substantive sections of the Bankruptcy Code that truly is peculiar to federal bankruptcy.

In addition, various district courts and bankruptcy courts have allowed a creditor to recover its post-petition attorneys' fees as part of its unsecured claim. *See, e.g., Liberty National Bank v. George*, 70 B.R. 312 (W.D. Ky. 1987) (claim for contractual attorneys' fees above the value of an oversecured creditor's collateral should be allowed as an unsecured claim); *In re Ladycliff College*, 56 B.R. 765 (S.D.N.Y. 1985) (award of post-petition fees under collection clause in contract as unsecured claim is not erroneous or contrary to law).

The conflict between the Ninth Circuit and these other courts cannot be permitted. Consistency among courts in a national bankruptcy system is of prime importance. Unless this Court resolves the issue, the award of post-petition fees as part of allowed claims in a particular case would depend on the venue of the proceeding rather

than the uniform rule of law. To subject debtors and creditors in general to this confusion goes against the national bankruptcy system's purpose of providing an orderly and predictable framework for resolution of bankruptcy claims.

IV.

THE NINTH CIRCUIT'S PER SE RULE DISTURBS THE DELICATE BALANCE OF POWER IN BANKRUPTCY PROCEEDINGS AND CREATES CONFUSION AS TO THE AWARD OF ATTORNEYS' FEES AS PART OF CREDITORS' CLAIMS IN BANKRUPTCY ACTIONS

The Ninth Circuit acknowledged that, "where a contract or statute provides for an award of attorneys' fees, a creditor may be entitled to such fees in bankruptcy proceedings. Such an award is governed by state law." *In re Fobian*, 951 F.2d at 1153. When claims are determined in bankruptcy, the debtor's and trustee's attorneys' fees are paid out of the *estate*. 11 U.S.C. § 330(a)(1) and 503(b)(2). The creditors' fees are borne by the individual creditor unless there is a contractual provision stating otherwise. If there is such a contractual attorneys' fee provision, state law governs its effect.

In *Fobian*, however, the Ninth Circuit created a *per se* federal rule which departs from this traditional understanding and intrudes upon the delicate balance of power between creditors and debtors. Before the broad rule announced in *Fobian*, if there was a contractual attorneys' fees clause, a creditor's attorneys' fees could become part of the creditor's allowed claim against the estate, and therefore the economic cost of litigation was borne, in part, by the estate. After *Fobian*, debtors and trustees

need not take the fees incurred by creditors into account when determining their strategy, because the creditor's costs do not become a claim against the estate if the issues litigated are "peculiar to federal bankruptcy law." Likewise, creditors may be forced to accept terms less favorable that the Bankruptcy Code would require because of the unrecoverable expense of challenging illegal reorganization plans such as the plan rejected by both the Bankruptcy Appellate Panel and the Ninth Circuit in *Fobian*.

Equally damaging is the new uncertainty created by the Ninth Circuit's decision that the issues under Sections 506 and 1225 before the court in *Fobian* were "issues peculiar to federal bankruptcy law." Petitioner did not initiate either the Chapter 12 case or the plan dispute; the Debtor's Chapter 12 plan proposed to strip the Petitioner of part of its claim and Petitioner simply defended its contractual claim. Essentially every action by a creditor in a bankruptcy is *both* an effort to enforce its contract (which is a claim under Section 506) *and* to resolve a bankruptcy issue, yet *Fobian* provides no guidance to courts or litigants as to what types of activity results in the award of recoverable fees. The Ninth Circuit's broad holding demonstrates the danger in having the award of attorneys' fees turn upon a court's decision as to whether that issue is "peculiar to federal bankruptcy law."

The national bankruptcy system cannot operate properly within this confusion. Courts and litigants should not be forced in every case to determine whether a particular issue is peculiar to bankruptcy law. Debtors and creditors should not be placed in a position where they cannot determine if attorneys' fees will become part of

the creditors' allowed claim. And, finally, the delicate balance of power between debtors and creditors inherent in the Bankruptcy Code, which generally leads to settlement of claim disputes, should not be changed without an analysis of the statutory policies behind awards of attorneys' fees as part of creditors' claims and the enforcement in bankruptcy of contracts, valid under state law, providing for their recovery.

V.

SECTION 506(b) OF THE BANKRUPTCY CODE DOES NOT PROHIBIT THE ALLOWANCE OF AN AWARD OF ATTORNEYS' FEES TO WESTERN FARM CREDIT BANK

A. Section 506(b) Does Not Prohibit An Undersecured Creditor From Adding Attorneys' Fees To The Unsecured Portion Of Its Claim.

The broad rule announced in *Fobian* makes no distinction whatsoever among fully secured claims, undersecured claims and unsecured claims. Some courts have held that because Section 506(b) provides for attorneys' fees to be made part of the *secured* claim of an *over*secured creditor, that is the only time attorneys' fees can be added to a claim. Undersecured and unsecured creditors are not entitled to add attorneys' fees incurred during bankruptcy proceedings to their claim, no matter what the contractual language. *See, e.g., In re Sakowitz, Inc.*, 110 B.R. 268, 275 (Bankr. S.D. Tex. 1989). This is an erroneous reading of the statute, and was in fact rejected by the Ninth Circuit in *Matter of 268 Ltd.*, 789 F.2d 674, 678 (9th Cir. 1986). The *Matter of 268 Ltd.* court wrote:

> "Our rejection of [Creditor's] construction of § 506(b) does not preclude it from seeking the contractual fees in excess of $20,000 as an unsecured claim. Section 506 establishes the requirements for a secured claim. Subsection (a) defines such claims. Subsection (b) states that under some circumstances 'there shall be allowed to the holder of such claim interest, fees, costs or charges. When read literally, subsection (b) arguably limits the fees available to the oversecured creditor. When read in conjunction with § 506(a), however, it may be understood to define a portion of the fees which shall be afforded secured status. We adopt the latter reading."

In re 268 Ltd., supra, 789 F.2d at 678. In ruling that fees may become part of the creditor's claim, the Ninth Circuit expressly acknowledged that Section 501 of the Bankruptcy Code "contemplates that undersecured creditors may pursue the unsecured portion of their claims as unsecured creditors." *Id.*

B. Given Fobian's Solvent Status, Western Farm Should Have A Claim For Its Attorneys' Fees.

Fobian is solvent. *Fobian,* 951 F.2d at 1150. When a debtor is solvent, courts have awarded unsecured creditors a claim for post-petition interest, despite the general rule to the contrary. *In re Walsh Construction, Inc.,* 669 F.2d 1325, 1330 (9th Cir. 1982) (pre-Bankruptcy Code Case). The Bankruptcy Code has provided that, where the debtor is solvent, post-petition interest on claims is available to creditors. 11 U.S.C. § 726(a)(5). Even courts which contend that undersecured and unsecured creditors are

not entitled to make attorneys' fees part of their unsecured claim have made an exception in the case of a solvent debtor. "This court is further of the opinion that attorneys' fees should be allowed where the Debtor is solvent (before and after the allowance) due to policy considerations akin to those with respect to the allowance of interest post-petition." *Sakowitz, supra,* 110 B.R. at 270; *see, In re Continental Airlines Corp., Inc.,* 110 B.R. 276 (Bankr. S.D. Tex. 1989) (awarding attorneys' fees to unsecured creditor of solvent debtor).

The broad, *per se* rule in *Fobian* makes no distinction between solvent and insolvent debtors. This failure to take Fobian's solvency into account is illustrative of the danger in announcing a broad rule that has no basis in the written language of the Bankruptcy Code and which has no guidelines for its implementation. The *Fobian* rule makes the orderly resolution of claims *less* likely rather than more likely, and introduces inconsistency into what should be a uniform system for bankruptcy cases.

CONCLUSION

Petitioner Western Farm Credit Bank prays that a writ of certiorari issue from this Honorable Court to review the judgment of the Court of Appeals for the Ninth Circuit in *In Re Fobian*. In the event that the petition is granted, Petitioner prays that the judgment of the Court of Appeals as to the award of attorneys' fees as part of Petitioner's claim be reversed and that the cause be remanded for proceedings consistent with this Court's ruling.

Respectfully submitted,

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APPENDIX A

In re Elmer FOBIAN and Elsie Fobian, Debtors.

Elmer FOBIAN and Elsie Fobian, Appellants,

v.

WESTERN FARM CREDIT BANK, Appellee.

No. 90-16313.

United States Court of Appeals, Ninth Circuit.

Argued and Submitted Nov. 6, 1991.

Decided Dec. 24, 1991.

Wayne B. Harbarger, III, Sacramento, Cal., for appellants.

Gloria M. Greene, Tennant, Greene & Dutra, Sacramento, Cal., for appellee.

Appeal from the Ninth Circuit Bankruptcy Appellate Panel.

Before FLETCHER, WIGGINS and KOZINSKI, Circuit Judges.

FLETCHER, Circuit Judge:

Elmer and Elsie Fobian appeal from the decision of the Bankruptcy Appellate Panel ("BAP") reversing the bankruptcy court's confirmation of their chapter 12 plan. They argue that the BAP erred in holding that the plan could not be confirmed because it did not meet the requirements of Section 1225 of the Bankruptcy Code.[1]

---

[1] Unless otherwise stated, all references to "sections" refers to the Bankruptcy Code, 11 U.S.C. § 101 et seq.

The Bank argues for affirmance of the BAP's decision, and asks that we award it attorneys' fees and costs.

We affirm the BAP's decision, but award the Bank only costs on appeal.

BACKGROUND

The Fobians are solvent Chapter 12 debtors. They are current on all obligations except a loan from the Bank. The Bank holds a promissory note secured by 70.5 acres of land located in Glenn County, California and stock in the Federal Land Bank Association of Northern California. After the Fobians filed their Chapter 12 petition, the Bank filed a Proof of Claim for $191,660.09. The Proof of Claim stated: "No security interest is held for this claim except Deed of Trust. Stock in FLBA of Northern California perfected pursuant to the Farm Credit Act of 1971." The Fobians made no objections to this Proof of Claim.

While the Fobians filed three plans, only the "First Amended Plan for Reorganization under Chapter 12" (the "Plan") was submitted for confirmation. The Bank filed objections to the plan and a confirmation hearing was held on June 27, 1989.

The Plan provided for treatment of the Bank's claim as follows:

> The "Distressed Property" consists of approximately 70.5 acres of rice land in Glenn County undersecured by a promissory note and deed of trust to FLB [the Bank] in the approximate sum of $190,000 (including interest and penalties). The Debtor also owes approximately 2 years real

> estate taxes to the County of Glenn on the property. The fair market value of the property is estimated by the Debtors to be $70,500.00. The Debtors would propose alternative treatments to the Secured Creditor.
>
> The first alternative is a refinancing of the debt and write-off of balance over the new principal of $70,500. The new obligation would carry 9.0% interest for a term of 40 years with annual payments beginning 12/31/90.
>
> The second alternative is that the Debtors will surrender the property pursuant to 11 USC 1225(a)(5)(C). Said surrender would be in full satisfaction of the amount allegedly due to the Secured Creditor.
>
> Under either alternative there would be *no* undersecured obligation owed to the secured creditor, no deficiency judgments and no net disposable payments to be made through the trustee. The Secured Creditor may elect their [sic] choice of alternative until the date and time set for the hearing on the Plan. If the Secured Creditor has not chosen their alternative by the date and time set for hearing on confirmation of the Plan, the Debtors may elect their choice of alternative.

The Bank did not elect either alternative. The Fobians then elected the second alternative, surrender of the property.

The Bank objected to confirmation of the Plan on the grounds that the plan did not take into consideration the unsecured portion of the Bank's claim, and did not comply with the requirements of Section 1225(a)(4). The Bankruptcy Court nonetheless confirmed the Plan in a

Memorandum Opinion and Order Including Findings of Fact and Conclusions of Law filed on August 7, 1989.

The BAP reversed, holding that because the Plan did not meet the requirements of Section 1225, it could not be confirmed.

STANDARD OF REVIEW

We review a bankruptcy court's conclusions of law *de novo*. Findings of fact are upheld unless they are clearly erroneous. *Rubin v. West (In re Rubin)*, 875 F.2d 755, 758 (9th Cir. 1989).

DISCUSSION

Because the Plan fails to comply in several ways with Section 1225, the BAP was correct in reversing the bankruptcy court's confirmation. We now analyze in some detail the treatment of the Bank's claim by the bankruptcy court and the Plan.

1. Section 506

In confirming the plan, the bankruptcy court stated that at the time of confirmation the extent to which the bank was secured was "uncertain." The bankruptcy court found that "it is clear that BANK has not yet become an unsecured creditor." Thus, the Bank could not invoke the protections Section 1225 provides for such claims. Looking in particular to description of the Bank's claim in the Plan itself, the BAP found that the bankruptcy court had erred in holding that the Bank held only a secured claim. The BAP was correct in this holding.

The BAP cited Section 506, which provides:

> (a) An allowed claim of a creditor secured by a lien on property in which the estate has an interest . . . is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property . . . and is an unsecured claim to the extent that the value of such creditor's interest . . . is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.

11 U.S.C. § 506(a). Section 506 required the bankruptcy court to determine whether the bank was both a secured and an unsecured creditor. Without doing so, the court could not apply the tests of Section 1225 to the plan.

II. Section 1225(a)(5)

The Fobians argue that the Bank has no unsecured claim under the plan as the Bank was offered the option of receiving the property securing its claim in full satisfaction of that claim. In support of this argument, the Fobians invoke Section 1225(a)(5), which provides:

> (a) Except as provided in subsection (b), the court shall confirm a plan if –
>
> > (5) with respect to each allowed secured claim provided for by the plan –
> >
> > > (C) the debtor surrenders the property securing such claim to such holder
> > >
> > > . . .

11 U.S.C. § 1225(a)(5).

As the Fobians note, cases have acknowledged the "theoretical possibility" of a surrender of property in satisfaction of a secured debt; however, such cases have also recognized that such a solution is unworkable in practical terms. Absent the provision of some additional protection to the creditor, it is impossible to ensure that the creditor will receive the full amount to which it is entitled, and only that amount. Surrender of the property may satisfy the secured claim. However, if the value of the property is less than the amount of the claim, the creditor may retain an unsecured claim for the difference. If the value of the property surrendered turns out to exceed the amount of the claim, the secured creditor receives a surplus to which it is not entitled. Thus, the court in *In re Durr* rejected a plan which provided for the transfer of real property in satisfaction of a secured claim. The *Durr* court noted that a plan "proposing a payment with tangible property" must provide both for a "surplus of value" or for a "margin of allowance" to ensure that the creditor received full value, and for a means of recapturing excess value the creditor might realize on disposition of the collateral. *In re Durr*, 78 B.R. 221, 225 (Bankr.D.S.D.1987). Because the plan at issue made no such provisions, it could not be confirmed. *Id., see also In re Indredland*, 77 B.R. 268, 274 (Bankr.D.Mont.1987) (approving plan which provided for transfer of property to secured creditor where the debtor had submitted a 5 year plan, and the creditor could return to the court for "redetermination of its claim" if it failed to realize the value of its claim on sale of the collateral).

In this case, the debtor's plan provides for neither the safeguard required by *Durr* nor the possibility of redetermination present in *Indreland*. While Section 1225(a)(5)

would extinguish the Bank's claim to the extent it was secured, the unsecured portion would survive.

III. Section 1225(a)(4)

Section 1225(a)(4) provides:

> (a) Except as provided in subsection (b), the court shall confirm a plan if –
>
> > (4) the value, as of the effective date of the plan, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under chapter 7 of this title under such date . . .

11 U.S.C. § 1225(a)(4).

Here, all parties acknowledged that the debtor had substantial net worth. Thus, in a chapter 7 liquidation, the Bank would be paid in full. However, the Plan makes no provision for the unsecured portion of the Bank's claim. Therefore, the Plan does not meet the requirements of Section 1225(a)(4). The BAP was correct in reversing confirmation for this reason.

IV. Section 1225(b)

Section 1225(b) provides:

> (b)(1) If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan unless, as of the effective date of the plan –

> (A) the value of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or
>
> (B) the plan provides that all of the debtor's projected disposable income to be received in the three-year period, or such longer period as the court may approve under section 1222(c), beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.

11 U.S.C. § 1225(b)(1).

Section 1225(b) does not provide an alternative to compliance with Section 1225(a); rather, each subsection must be satisfied independently. *In re Willingham,* 83 B.R. 552, 553 (Bankr.S.D.Ill.1988).

Here, the Plan provides for no payment to the Bank in satisfaction of its unsecured claim. It also fails to provide for any portion of the Fobians' income to be applied to payments to the Bank. Thus, the Plan fails to meet the requirements of Section 1225(b). The BAP was correct in reversing confirmation on these grounds.

V. Award of Attorneys' Fees and Costs to the Bank

The Bank asks for an award of attorneys' fees and costs. It cites provisions in the promissory note and the deed of trust executed in relation to the loan which provide for the payment of fees and costs incurred in collection of amounts due or enforcement of rights.

A. Costs on Appeal

Bankruptcy Rule 8014 provides, in relevant part: "Except as otherwise provided by law, agreed to by the parties or ordered by the district court or bankruptcy appellate panel, costs shall be taxed against the losing party on appeal." Bankruptcy Rule 8014. Thus, we award the Bank its costs on its appeals before the BAP and before this court.

B. Attorneys' Fees at all levels; Costs in the Bankruptcy Court

Where a contract or statute provides for an award of attorneys' fees, a creditor may be entitled to such fees in bankruptcy proceedings. Such an award is governed by state law. *Collingwood Grain, Inc. v. Coast Trading Co. (In re Coast Trading Co.)*, 744 F.2d 686, 693 (9th Cir.1984); *Merced Production Credit Ass'n v. Sparkman (In re Sparkman)*, 703 F.2d 1097, 1099 (9th Cir.1983).

However, where the litigated issues involve not basic contract enforcement questions, but issues peculiar to federal bankruptcy law, attorney's fees will not be awarded absent bad faith or harassment by the losing party. *Coast Trading*, 744 F.2d at 693 (refusing to award fees where creditor brought a nondischargeability action); *Grove v. Fulwiler (In re Fulwiler)*, 624 F.2d 908, 910 (9th Cir.1980) (refusing to award fees for creditor's action under Section 546); *see also Johnson v. Righetti (In re Johnson)*, 756 F.2d 738, 741-42 (9th Cir. 1985) (because creditor's request for relief from the automatic stay pursuant to Section 362(d) was not an "action on the contract,"

debtor was not entitled to attorneys' fees for defense against the request).

Here, litigation involved solely issues of federal bankruptcy law: the Bank sought proper application of Sections 506 and 1225. This was not a traditional "action on the contract." "[T]he question of the applicability of the bankruptcy laws to particular contracts is not a question of the enforceability of a contract but rather involves a unique, separate area of federal law." *Coast Trading*, 744 F.2d at 693. Thus, we decline to award the Bank attorneys' fees for its litigation of this case at all levels, and limit the award of costs to costs incurred on appeal.

AFFIRMED.

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

In re: ELMER FOBIAN and ELSIE FOBIAN, Debtors,	
ELMER FOBIAN and ELSIE FOBIAN, Appellants, v. WESTERN FARM CREDIT BANK, Appellee.	No. 90-16313 BAP No. EC-89-1765 ORDER (Filed Feb. 4, 1992)

Before: FLETCHER, WIGGINS, and KOZINSKI, Circuit Judges,

The petition for rehearing is denied.

APPENDIX B

UNITED STATES BANKRUPTCY APPELLATE PANEL
OF THE NINTH CIRCUIT

In re ELMER FOBIAN, ELSE FOBIAN, Debtors.	BAP NO. EC 89-1765 ROAs BK. NO. 288-07673-A-12 Memorandum (Filed Aug. 16, 1990)
WESTERN FARM CREDIT BANK Appellant, v. ELMER FOBIAN, ELSE FOBIAN, Appellees.	

Argued and Submitted on February 15, 1990
at Sacramento, California

Filed AUG 16 1990

Appeal from the United States Bankruptcy Court
for the Eastern District of California

Honorable Loren S. Dahl, Bankruptcy Judge, Presiding

Before: RUSSELL, OLLASON, and ASHLAND, Bankruptcy Judges.

Creditor Western Farm Credit Bank appeals from an order confirming the debtor's first amended plan of

reorganization.[1] The plan did not meet the requirements of 11 U.S.C. Section 1225 because it failed to provide for Western Farm Credit Bank's unsecured claim. WE REVERSE and REMAND.

I.

FACTS

The debtors, Elmer and Else Fobian (Fobians) are solvent Chapter 12 debtors having a net worth of approximately $480,000. The debtors are current on all obligations except a certain loan No. 236077-2 to Western Farm Credit Bank (Western). Western holds a promissory note for the principal sum of $155,000 secured by 70.5 acres of rice land located in Glenn County, California and stock in the Federal Land Bank Association of Northern California. Western filed a Proof of Claim for the amount owing, $186,864.18, on December 20, 1988. Approximately $80,000 of this is unsecured.[2] No objections were made to the Proof of Claim.

---

[1] According to the Fobian's valuation, the fair market value of the land is $70,500. According to Western's valuation, the fair market value of the land is $110,000.

[2] The court's "Memorandum Opinion and Order Including Findings of Fact and Conclusions of Law" was entered August 7, 1989. On August 17, 1989 Western Farm Credit Bank filed a Notice of Appeal "from the final Order of the Bankruptcy Court on the Creditor's Objections to Confirmation of the First Amended Plan as entered on August 7, 1989." The "Order of Confirmation of Debtor's Plan of Reorganization" was entered on August 25, 1989. It is clear that Western is appealing from the Order confirming the Debtor's plan.

The Fobians filed three plans, but only the "First Amended Plan for Reorganization Under Chapter 12" was submitted for confirmation (the plan) and is the subject of this appeal. Western filed objections to the plan and a confirmation hearing was held on June 27, 1989. Western objected to it's treatment as the Class 5 Creditor on the real property loan No. 236078-0.

The First Amended Plan of Reorganization provided for Western's Class V claim as follows:

> The "Distressed Property" consists of approximately 70.5 acres of rice land in Glenn county *undersecured* by a promissory note and deed of trust to FLB in the approximate sum of $190,000 (including interest and penalties). The Debtor also owes approximately 2 years real estate taxes to the County of Glenn on the property. The fair market value of the property is estimated by the debtors to be $70,500.00. The debtors would propose alternative treatments to the secured creditor.
>
> The first alternative is a refinancing of the debt and write-off over the new principal of $70,500. The new obligation would carry 9.0% interest for a term of 40 years with annual payments beginning 12/31/90.
>
> The second alternative is that the Debtors will surrender the property pursuant to 11 U.S.C. 1225(a)(5)(c). Said surrender would be in full satisfaction of the amount allegedly due to the Secured Creditor.
>
> Under either alternative there would be *no* under-secured obligation owed to the secured creditor, no deficiency judgments and no net disposable payments to be made through the

> trustee. The Secured Creditor may elect their choice of alternative until the date and time set for the hearing on the Plan. If the Secured Creditor has not chosen their alternative by the date and time set for hearing on confirmation of the Plan, the Debtors may elect their choice of alternative.

Appellants Excerpts, Exhibit T at 173.

Western objected to the plan on the grounds that it proposed to pay nothing on the unsecured portion of their claim. Western argued that under 11 U.S.C. Section 1225(a)(4) the court could confirm the Fobian's plan only if the value of the property received on their allowed unsecured claim was not less than the amount they would receive under a Chapter 7 liquidation. According to an updated financial statement of the debtors, the Fobians had a net worth of $481,000. Appellants Excerpts, Exhibit S at 121-122. Since the debtor is solvent, Western would be paid in full on the loan under a Chapter 7 liquidation.

The court confirmed the plan in a Memorandum Opinion and Order Including Findings of Fact and Conclusions of Law filed on August 7, 1989. The court found that Western was not an unsecured creditor at the time of confirmation of the plan, although it may become an unsecured creditor at some time in the future. At such a time, Western would have to then pursue collecting any deficiency on the loan. The court disallowed a declaration by Western's appraiser as to the value of the property and refused to determine whether Western had unsecured status because the hearing was not noticed as a valuation hearing. The court found that it was not necessary for the

plan to meet the requirements of Section 1225(a)(4) because Western was not an unsecured creditor.

II.

ISSUES

1. Whether the bankruptcy court erred in holding that Western Farm Credit Bank is not an unsecured creditor.

2. Whether the bankruptcy court erred in holding that 11 U.S.C. Section 1225 did not apply to confirmation of the plan.

III.

STANDARD OF REVIEW

Findings of fact are reviewed under a clearly erroneous standard and conclusions of law are reviewed *de novo*. *Ragsdale v. Haller*, 780 F.2d 794, 794 (9th Cir. 1986); Bankr. R. 8013.

IV.

DISCUSSION

A. WESTERN FARM CREDIT BANK HAS AN ALLOWED UNSECURED CLAIM

Western filed a Proof of Claim for $186,864.18 on December 20, 1988. Section 502(a) provides:

> *Allowance of claims or interests.*
>
> (a) A claim or interest, proof of which is filed under section 501 of this title, is deemed

> allowed, unless a party in interest, including a creditor of a general partner in a partnership that is a debtor in a case under chapter 7 of this title objects.

No objections were made to Western's Proof of Claim, therefore it is deemed allowed.

Section 506(a) provides:

> *Determination of secured status.*
>
> (a) An allowed claim of a creditor secured by a lien on property in which the estate has an interest, . . . is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property, . . . *and is an unsecured claim to the extent that the value of such creditor's interest* . . . is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or plan affecting such creditor's interest.

"Subsection (a) of this section separates an undersecured creditor's claim into two parts – he has a secured claim to the extent of the value of his collateral; he has an unsecured claim for the balance of his claim." 11 U.S.C. § 506(a), House Report (Reform Act of 1978) (Norton 1990).

Western contended in the trial court and reasserts here that its claim is secured for the value of the 70.5 acres of rice land, and unsecured for approximately $80,000. The bankruptcy court disagreed with Western:

> In this regard, the BANK's contention is incorrect. The BANK'S proof of claim filed herein shows that the loan is evidenced by a promissory note which contains language referring to a deed of trust of the same date on the Glenn County property. In fact the proof of claim states that the obligation is not only secured by the deed of trust but also stock in FLBA of Northern California. These facts are not disputed by the debtors. At the present point in time, the BANK may be oversecured, undersecured or exactly secured. Which, is yet unknown. The court only knows from the evidence before it that BANK is secured but not to what extent.

Appellants Excerpts, Exhibit J at 33.

The evidence before the court included a statement in the plan in which the debtor admits that Western is an undersecured creditor and that the fair market value of the property was $70,500. The court disallowed Western's evidence of a fair market value of $110,000, but under either figure Western has an unsecured claim of at least $80,000. Valuation of secured and unsecured claims at a hearing on confirmation of a plan is necessary for determining whether claims receive proper treatment in the proposed plan. *See In re Bremer*, 104 Bankr. 999 (Bankr. W.D. Mo. 1989); *In re Danelson*, 77 Bankr. 261 (Bankr. D. Mont. 1987).

Western's Proof of Claim states "[t]his claim is a general unsecured claim, except to the extent that the security interest, if any, described in paragraph 9 is sufficient to satisfy the claim." Paragraph 9 provides that "[n]o security interest is held for this claim except Deed

of Trust recorded 6/4/82; capital stock of FLBA of Northern California created and perfected pursuant to the Farm Credit Act of 1971." Appellant' Excerpts, Exhibit W at 196. No evidence of the value of the FLBA stock was presented. Additionally, it is not clear whether the stock would be available for surrender under the Farm Credit Act. *See In re Greseth*, 78 Bankr. 936, 942-43 (D. Minn. 1987).

There was no dispute at the trial that the value of the land was less than the debt it secured. Mr. Harbarger, counsel for the Fobians so stated at trial during the following colloquy:

> THE COURT: I guess Miss Greene [Counsel for Western] is saying that as to the amount that the property is worth, fair market value is less than the total amount of the debt. They are unsecured as to that amount, right.
>
> Is that what you're saying?
>
> MISS GREENE: Yes.
>
> THE COURT: What is your response to that?
>
> MR. HARBARGER: If we did a (b)(5) program, that would be true. But if we are in here arguing about what the fair market value of the land, Judge, the balance will be unsecured. The balance will be unsecured. Then it's right. But that's not one of the options the Debtor is giving the creditor.
>
> Either agree at this price or take it back. "I" or "I". We don't care. "I" is not one of the options. We don't want an unsecured creditor.

Appellant's Excerpts, Exhibit K at 51.

To hold that Western has only a secured claim ignores that plain language of Section 506(a). It is obvious that Western has an unsecured claim without determining to what extent. *See In re O'Farrell*, 74 Bankr. 421, 423 (Bankr. N.D. Fla. 1987) (Upon the court's valuation of property and the debtors' return of certain collateral to F.L.B. as proposed, any deficiency due F.L.B. shall be treated as an unsecured claim by the debtor's plan.)

We disagree with the bankruptcy court's conclusion that Western has only a secured claim and hold that as a matter of law, according to the plain language of Section 506(a), Western has both a secured and an unsecured claim. The issue of the extent of the unsecured claim is not before this Panel and we make no finding as such.

B. THE PLAN VIOLATES 11 U.S.C. SECTION 1225

Western alleges that it was improper for the bankruptcy court to confirm the Plan where it did not meet the requirements of Section 1225. Section 1225(a) sets forth the mandatory provisions for confirmation of the debtor's plan. Section 1225(a) provides in pertinent part:

> *Confirmation of plan.*
>
> (a) *Except as provided in subsection (b),* the court shall confirm a plan if –
>
> (4) the value, as of the effective date of the plan, of property to be distributed under the plan on account of each allowed *unsecured* claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under chapter 7 of this title on such date;

(5) with respect to each allowed secured claim provided for by the plan –

(A) the holder of such claim has accepted the plan;

(B)(i) the plan provides that the holder of such claim retain the lien securing such claim; and

(ii) the value, as of the effective date of the plan, of property to be distributed by the trustee or the debtor under the plan on account of such claim is not less than the allowed amount of such claims; or

(C) the debtor surrenders the property securing such claim to such holder;

Western contends that the Plan does not meet the Section 1225(a)(4) "best interest" test. *See In re Nielsen*, 86 Bankr. 177 (Bankr. E.d. Mo. 1988) (surveying the interpretation and application of Section 1225(a)(4)). Under that subsection, the plan may only be confirmed if Western would receive not less under the plan than under a Chapter 7 liquidation. The evidence before the court was that the Fobians had a net worth of over $480,000, much of which were liquid assets.[3]

---

[3] The updated financial statement prepared by the Fobians and submitted to Western on March 1, 1988 and the testimony of Mr. Fobian at a 2004 examination on April 10, 1989 indicate that the Fobians had total assets of $875,450 and total liabilities of $394,000 for a net worth of $481,000. This evidence was before the bankruptcy court during the hearing on confirmation of the plan. Appellant's Excerpts, Exhibit S at 121-22.

Western's debt would be paid in full upon a Chapter 7 liquidation but the plan does not provide for any payment of the unsecured debt. A plan cannot be confirmed where the debtors have sufficient assets yet propose to pay nothing to the unsecured creditor because it does not satisfy Section 1225(a)(4). *In re Novak*, 102 Bankr 22, 23 (Bankr. E.D.N.Y. 1989) "A farmer's plan cannot be confirmed if it fails to comply with 11 U.S.C. § 1225(a)(4)." *In re Nielsen*, 86 Bankr. 177, 178 (Bankr. E.D. Mo. 1988).

Western correctly contends that as the holder of an allowed secured and unsecured claim, the surrender of the property alone extinguished only the secured claim. The Fobians attempt to strip Western of the protections afforded unsecured creditors by Section 1225(b).

However, Section 1225(a) is subject to subsection (b) which provides that:

> (b)(1) If the trustee or the holder of an allowed *unsecured* claim objects to the confirmation of the plan, then the court may not approve the plan unless, as of the effective date of the plan –
>
> > (A) the value of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or
> >
> > (B) the plan provides that all of the debtor's projected income to be received in the three year period, or such longer period as the court may approve under section 1222(c), beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.

Subsection (b) is separate from subsection (a) and sets forth an additional requirement that must be met if an unsecured creditor objects to confirmation of the plan. *In re Willingham,* 83 Bankr. 552 (Bankr. S.D.Ill. 1988). Neither requirement of Section 1225(b) was met by the plan. The property was less than the amount of Western's claim but there was no provision in the plan for any of the debtor's projected disposable income to be paid to Western.

"It is true Congress has exhibited a desire to keep the family farmer in operation, but *only* if the farmer complied with the standards set forth in Chapter 12, and in particular, section 1225." *In re Nielsen,* 86 Bankr. at 178.

The Fobian's plan failed to meet the mandatory requirements of Section 1225, therefore, we REVERSE the confirmation of the Plan.

V.

CONCLUSION

We hold that as a matter of law Western Farm Credit Bank has both an allowed secured and unsecured claim under 11 U.S.C. Section 506(a). The requirements of Section 1225 were violated where the solvent Chapter 12 debtor's plan failed to provide for the unsecured claim that Western holds. Therefore, WE REVERSE the confirmation of the debtor's plan.

APPENDIX C

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA

In re	No. 288-07673-A-12
ELMER FOBIAN and ELSE FOBIAN,	Motion No.
	Date Filed: May 16, 1989
Debtor(s).	Of: Objection to Confirmation of First Amended Plan
	(Filed Aug. 7, 1989)

MEMORANDUM OPINION AND ORDER INCLUDING FINDINGS OF FACT AND CONCLUSIONS OF LAW

WESTERN FARM CREDIT BANK (BANK) filed objections on May 16, 1989, to confirmation of debtor's first amended plan (plan) in this Chapter 12 case. Hearings on the objections and on confirmation were held June 27, 1989. At the outset, the court advises counsel that post-hearing documents filed by the parties are not being considered.

The debtor's have two outstanding loans with BANK. The BANK concedes that the first loan is fully secured by the "Home Ranch", and the payments are current. The second loan (Glenn) which has an approximate balance of $190,000.00 is secured by rice land in Glenn County and is delinquent. The BANK objects to the proposed treatment of this loan in debtor's plan contending *inter alia* that the plan fails to address the unsecured

portion of Bank's claim under the Glenn loan. Bank contends that as to this loan it is secured for $110,000.00 and unsecured for $80,000.00. It also asserts other objections which will be discussed later herein but, first it is necessary to examine its contention that at present its Glenn loan is both secured and unsecured.

In this regard, the BANK'S contention is incorrect. The BANK's proof of claim filed herein shows that the loan is evidenced by a promissory note which contains language referring to a deed of trust given to secure its payment and is secured by a deed of trust of the same date on the Glenn County property. In fact the proof of claim states that the obligation is not only secured by the deed of trust but also stock in FLBA of Northern California. These facts are not disputed by the debtors. At the present point in time, the BANK may be oversecured, undersecured or exactly secured. Which, is yet unknown. The court only knows from the evidence before it that BANK is secured but not to what extent. Nor is a determination of that fact before the court *sub judice.* The BANK is apparently trying to "bootstrap" its contention by filing a declaration of LOUIS VENTURINI, a BANK employee, wherein he expresses an opinion of value of the subject collateral. This hearing on BANK's objections were in connection with a confirmation hearing. It was not noticed as a valuation hearing and accordingly the VENTURINI declaration, which would be seriously questioned in any event because of his bias and lack of demonstrated qualifications, will be disregarded. The BANK did not timely accept debtor's "first alternative" as set forth under Class 5 in the plan, hence the "second alternative" surrender of the property pursuant to 11 U.S.C.

§ 1225(a)(5)(C) becomes effective upon confirmation of the plan. Upon the debtors surrender of the Glenn property to BANK pursuant to 11 U.S.C. § 1225(a)(5)(C), steps can be taken by BANK as stated in 5 Collier on Bankruptcy, 15th Ed. ¶1225.02, page 1225-9,10, "If there is a deficiency remaining after the disposition of the surrendered collateral, the creditor would be entitled to an allowed unsecured claim for that amount. The debtor and creditor could also otherwise agree or the creditor could accept the collateral in full satisfaction of its claim."

From the foregoing, it is clear that BANK has not yet become an unsecured creditor. It may never. But if it does at some later time, it may then pursue its rights as such.

The BANK also objects contending that the plan does not comply with Bankruptcy Code Section 1225(a)(4). This is the "best interests" test to be invoked for the protection of unsecured creditors. Because BANK is not presently an unsecured creditor, it has no standing to make this objection.

Further, the BANK urges that the plan has not been proposed in good faith as required by Section 1225(a)(3). The court has read the 2004 examination of ELMER FOBIAN taken April 10, 1989, but finds nothing therein which would support a finding that the plan was not proposed in good faith. In short, admissible evidence is lacking to support this objection.

The last objection recites that the required 25-day notice of the confirmation hearing was not given. At the most the notice was insufficient by three days, depending on the applicability of FRCP 6(e). This does not appear to be an objection *per se* and at least as to this objecting

creditor, it apparently did not affect it, for its counsel presented its objections fully and timely.

This opinion shall constitute findings of fact and conclusions of law. The BANK's objections to confirmation are denied. Counsel for the debtors will submit an order of confirmation.

IT IS SO ORDERED.

DATED: AUG 7 1989

/s/ Loren S. Dahl
Chief Judge, United States
Bankruptcy Court

I certify that on AUG 7 1989, a copy of the foregoing Memorandum Opinion and Order was mailed to the following:

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WAYNE B. HARBARGER, III, ESQ.
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(Atty for Debtors)

/s/ Nancy Williams

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Attorney for Debtor
ELMER FOBIAN and ELSE FOBIAN

IN THE UNITED STATES BANKRUPTCY COURT
IN AND FOR THE EASTERN DISTRICT
OF CALIFORNIA

In Re:	Case No. 288-07673-A-12
ELMER FOBIAN and ELSE FOBIAN Debtor	ORDER OF CONFIRMATION OF DEBTOR'S PLAN OF REORGANIZATION
	(Filed Aug. 25, 1989)

On June 27, 1989 at 2:00 p.m. in Department A, the Debtor's Plan of Reorganization was heard by the Honorable Loren Dahl. After considering the Debtor's Plan of Reorganization, written objections thereto, oral arguments by all interested counsel and the Trustee, the Court makes the following Order Confirming and Amending the Debtor's Plan of Reorganization:

1. Debtors herein are qualified as a Family Farmer to file a Chapter 12 within the meaning of 11 USC section 101 (17);

2. Debtors have complied with all notice requirements and has timely filed its Plan of Reorganization;

3. The Debtors Plan was proposed in good faith and complies with the provisions of Chapter 12 as and with all other applicable statutes and Rules of Court;

4. DISCHARGE OF DEBTOR:

Upon payment of the claims to the Class 1 creditors and payment of $2000.00 to the Chapter 12 trustee and execution of a quit claim deed to the Class 5 creditor, the Debtor shall be discharged.

5. PRIOR CLAIMS BARRED:

Since no adversary actions were filed within the statutory period, all claims which were listed and treated in the Debtor's plan of reorganization are forever barred from further action against the Debtor save those creditors and claims classified as class 3 creditors which may exercise their contractual rights in the event of default if they do not conflict with applicable state law.

6. CLASS 1 CLAIMS:

The Debtors shall pay to the class 1 creditors their billings upon presentation and without further Order of this Court.

7. CLASS 2 CREDITOR:

The Debtor's counsel shall transmit a check held in trust for the trustee in the amount of $2,000.00 to the trustee upon receipt of an endorsed Order of Confirmation.

8. CLASS 3 & 4 CREDITOR:

The Debtor shall maintain the obligation in a current condition.

9. CLASS 5 CREDITOR:

The Debtor shall execute a Quit Claim Deed to the real property to the lienholder, Western Farm Credit Bank. The property as tendered shall constitute full satisfaction of the indebtedness owed to Class 5 Creditor on the real property loan no. 236078-0.

10. UNSECURED CREDITORS:

The Debtors have no unsecured creditors.

11. RETENTION OF JURISDICTION:

The Court shall retain jurisdiction to determine:

(a) allowance or disallowance of claims;

(b) determination of professional compensation;

(c) such other matters as the Debtor may bring before the Court.

12. EFFECTIVE DATE OF THE PLAN:

The effective date of the Plan shall be 30 days after the execution of the ORDER OF CONFIRMATION of the Plan.

DATED: AUG 25 1989

LOREN S. DAHL
LOREN S. DAHL
U.S. BANKRUPTCY JUDGE